THAILAND

Environment

Since the crisis broke in mid-1997 in Thailand and spread across the region, market confidence in the baht and in the Thai economy more generally was badly damaged, directly and indirectly affecting the economy's human resources. The economic restructuring programmes to deal with the crisis, must be strong and comprehensive.

Thailand has introduced a series of measures, with support from the International Monetary Fund, the World Bank, the Asian Development Bank, the International Labour Organisation, and bilateral sources including the Japanese Government to overcome its currency and financial crisis, and to build strong fundamentals for the resumption of growth in 1999. To date, many encouraging signs of stability have emerged, reflecting stronger market conditions.

Macroeconomic Framework and Policy

After having enjoyed a real compound annual growth rate of 9.6 per cent between 1986 and 1996, Thailand suffered a sharp economic downturn with the combination of currency and financial crises in 1997 as a result of the unsuccessful defense of the currency and the weak banking system. Thailand faced four major macroeconomic problems:

1. Net international reserves were depleted because of the unsuccessful defence of the Thai baht.
2. There were systemic problems in the financial sector.
3. The real sector faced a serious liquidity shortage.
4. Regional economic turmoil was a significant constraint in the economy's ability to resolve its economic difficulties.

Therefore, the Government has taken a systematic but flexible approach in addressing these problems and strictly adhered to the economic programme agreed with the International Monetary Fund. To date, Thailand has made steady progress in resolving its problems.

The economy has been weaker than anticipated, with a decline in real GDP of 0.4 per cent and 8 per cent in 1997 and 1998, respectively. A number of external and domestic factors have contributed to this performance. The continued unsettled conditions in the region are a key factor, reducing export values below previous projections, and delaying recovery in private capital flows. Domestically, both consumption and investment demand have been weaker than previously expected.

Nevertheless, in recent months financial conditions have improved. The strengthening of market confidence has extended beyond the exchange rate to declining inflation and interest rates, a rise in the stock market, and a leveling off in indicators of production and demand.

Under the momentum of the policy initiatives, output could begin rising steadily during 1999. Although growth for the year as a whole is likely to be about 1 per cent, this implies a fairly rigorous rebound, reaching 3–4 per cent in the fourth quarter of 1999 relative to the fourth quarter of 1998. The external reserves position will be further strengthened, while inflation will be further reduced.

Fiscal Policy

Thailand adopted an expansionary fiscal policy for fiscal year 1998/99 to stimulate domestic demand and employment and to finance economic and financial restructuring. The overall public sector deficit for fiscal year 1998/99 was increased to 5 per cent of GDP, compared to about 3 per cent in the previous fiscal year. Note that these deficit targets do not include the fiscal cost of financial restructuring.

In order to achieve its targets, Thailand has implemented various revenue and expenditure measures including tax refunds to exporters and corporations, postponement of both the payment of corporate income tax and the remittance of state enterprises' profits, and removal of tax disincentives to corporate debt restructuring. Furthermore, as for fiscal year 1998/99, Thailand plans to use foreign financing, about 1 per cent of GDP, to support specific spending projects directed toward social safety net and related labour-intensive investment projects. Thailand will also continue to accelerate the disbursement of budgetary and non-budgetary expenditures.

The two major measures to restructure the financial system that have incurred fiscal costs include: (1) the restructuring of the debt of the Financial Institution Development Fund (FIDF); and (2) the 14th August 1998 Financial Restructuring Package. Such fiscal costs include the principal and interest payments of government bonds issued for the purposes of restructuring.

The total value of the bonds issued for the restructuring of the FIDF is 500 billion baht. The issuance of all the FIDF's bonds will be completed within fiscal year 1998/99. The total value of the bonds for the 14th August package is 300 billion baht, and they will be issued in fiscal years 1998/99 and 1999/2000.

As noted above, the deficit targets do not include the fiscal costs of financial restructuring. Such restructuring tasks will involve fiscal burdens for the central government in the national budget each year until the debts are fully amortized. In fiscal year 1998/99, the government will fiscalise financial restructuring costs of around 1.5 per cent of GDP. Preliminary estimates suggest that the interest costs associated with all restructuring operations could average around 3–4 per cent of GDP on an annual basis over the next few years.

Monetary and Exchange Rate Policy

When the magnitude of the net official reserves was disclosed for the first time in August 1997, showing the steep decline from over US$33 billion at the end of 1996 to less than US$1 billion at end-August 1997, as a result of the unsuccessful defense of the baht, the market panicked. Even though the government came up with a strong stabilization programme, supported by the IMF, to regain international confidence, the baht continued to lose value.

Thailand set the highest priority on regaining market confidence and stabilising the currency value by implementing a tight and prudent monetary policy, which so far has delivered very positive outcomes in terms of controlling inflation, stabilising the exchange rate, and lowering interest rates. The increase in international confidence is reflected in the appreciation of the baht from 53.7 baht to the US dollar in January 1998 to around 36 baht to the US dollar in December. Thailand has also been able to reduce interest rates without sacrificing exchange rate stability. The money market rates are now in the 4–6 per cent range, below those prevailing prior to the crisis. Bank lending rates have also started to decline, allowing for emerging recovery.

In view of weak bank lending, Thailand is now improving terms and mechanisms underlying loans for export financing, supported by the ADB and the Export-Import Bank of Japan, to remove bottlenecks in the expansion of credit to viable firms. Moreover, with the cooperation of the World Bank, a programme has been adopted to recapitalise and strengthen the operation of the specialized financial institutions and their regulatory framework, in order to expand their operations to sectors such as low-income housing and small borrowers.

External Sector

The balance of payment's position of Thailand since the crisis broke has been mixed with rapid adjustments in both the current and capital accounts. The deteriorating international situation and falling export prices have dampened export values for Thai goods and services and resulted in higher volatility in the rollover rate of maturing liabilities. Nevertheless, the current account balance of 1998 is estimated at US$13.5 billion in surplus or about 11 per cent of GDP, with adjustment coming mostly from the import side. With falling export prices from weaker overseas demand offsetting the relatively slight increase in export volume, the export value in dollar terms decreased by –3.1 per cent this year. On the import side, the ongoing recession sharply reduced the value of imports, down 32 per cent in 1998. The current account balance is expected to record a surplus of about US$11 billion or 8.5 per cent of GDP in 1999, based on continued strength in export volumes and a possible rebound in import demand.

The capital account balance position in 1998 is expected to record a larger deficit despite an increase of FDI and a recent rebound in the stock market. Regarding the capital account in 1999, the deficit is likely to decrease, as the large stock of offshore forward and swap obligations should have been settled by end-1998 and the ongoing corporate debt restructuring package from 1998 will stimulate significant inflow of foreign direct investment. Reserves will continue to provide more than full coverage of short-term debt and are projected to reach US$32 to 34 billion at the end of 1999.

Thailand's total external debt at end 1998 is around US$86 billion. Although the total sum of external debt has not changed much, its composition has changed markedly. Short-term private debt decreased by 25 per cent (from US$34.3 billion to US$25.9 billion). The reserves/private short-term debt ratio has increased from 0.79 in 1997 to 1.1 in 1998. External debt of the public sector includes use of credit of the IMF and other monetary authorities.

Corporate Debt Restructuring

The process of corporate debt restructuring is an integral part of the restructuring of the non-performing loans, and hence of the overall financial system. To this end, the Bank of Thailand, in cooperation with the five associations, namely the Board of Trade, Federation of Thai Industries (representing debtor companies) and the Thai Bankers' Association, Association of Finance Companies, and the Foreign Banks' Association (representing the creditor groups) have set up a Corporate Debt Restructuring Advisory Committee (CDRAC). On 3rd August 1998, these associations signed on to a Framework for Corporate Debt Restructuring—the so-called Bangkok Approach, modelled along the London Approach.

Progress of CDRAC

On 13th October 1998, the CDRAC accepted 200 target cases of debt workouts proposed by the member associations. These target cases involve 353 companies with debt and overdue obligations totaling 674,326 million baht. The cases have been proposed and accepted as they involve complicated multicreditor-types of debt restructuring that require an outside mediator role. As of 15th December, 1998, five cases have successfully agreed on the terms of the restructuring: a local cement company, two steel companies, a mining company, and a telecommunications firm. The Committee is also closely monitoring the progress on the amendments of the various tax and fee structures for the transfer of ownership of assets (underlying collateral) that would facilitate the process of debt restructuring. Subsequently, the Joint Public-Private Sector Committee established a debt restructuring forum at the provincial level to be chaired by provincial governors.

Separately, financial institution creditors and debtors are also negotiating simpler debt restructuring cases and are required to report the results to the authorities. As of end-October 1998, financial institutions had completed 660 cases of debt restructuring, totaling 36,557 million baht (comprising of 9,707 million baht in the manufacturing sector; 3,355 million baht in construction; 6,189 million baht in real estate; 361 million baht in the export sector; and 16,945 million baht in other sectors). There are 2,390 other cases still in the process of restructuring, totaling 569,484 million baht.

Elimination of Tax Disincentives

Thailand is committed to facilitating the process of corporate debt restructuring through tax and legal reforms. Toward this end, the Government has eliminated impediments to restructuring by removing tax disincentives, with appropriate safeguards and applicable only to restructuring plans consistent with the Bank of Thailand regulations. These apply to all creditors who participate in a restructuring agreement with a financial institution.

Legal Amendments

The market-based strategy to corporate debt restructuring can only succeed if the incentive structure drives both debtors and creditors to accelerated negotiation and resolution. Thus, it remains crucial to strengthen bankruptcy legislation and to reform judicial foreclosure proceedings and secured lending legislation as much as possible. Legislative action has been taken on bankruptcy, enforcement of mortgages and broadening the range of assets that can serve as collateral.

Market Opening Policy

Privatization of state enterprises remains the Government's intention, in order to increase the role of the private sector in the economy which can make a significant contribution to solving the crisis, increasing efficiency in the use of resources, and improving the welfare of all Thai citizens.

Legislative action has been taken to improve transparency in the process of approving foreign investment in land and businesses.

The Labour Market and Wage Employment

In 1998, total employment stood at 30.8 million, reflecting a decline of 812,000, or 2.6 per cent, from the previous year. The number of workers outside the agricultural sector fell by 618,000, a 3.6 per cent reduction, while in the agricultural sector employment declined by 194,000. As consequence, the number of unemployed workers stood at 1.3 million, representing a 4 per cent unemployment rate, a sharp increase from the previous year's figure of 1.9 per cent. The unemployment rate did not increase substantially as the number of underemployed (that is, workers who work less than 35 hours per week and are available for work) rose significantly, and is estimated at 885,000 in the year 1998. The sectors in which there were large layoffs included construction, restaurants and hotels, small retail shops and electrical appliance repair.

Job terminations in the month of August 1998, rose sharply as a consequence of the amended labour law and the contribution schemes for old age pensions and child care allowances under the Social Security Act, which prompted decisions to lay off workers before the Acts became effective in December 1998.

The minimum wage rate was raised by approximately 3 per cent, effective 1st January 199 , as a result of the agreement made at the end of the previous year. There was no adjustment in the minimum wage rate during 1998, despite the acceleration in inflation.

Policies in Place

Employment of Workers

In Thailand, 80 per cent of the labour force is in the agricultural sector. After the harvest season, 40 per cent of the workers in this sector usually move to work in the industrial sector for a short period of 3–5 months. Therefore, the emergency policy is to speed up the rate of growth of employment, both in agriculture and outside of the agricultural sector.

In implementing its policy, the Government is keen on sustaining the existing jobs by giving assistance to maintain enterprises. In the meantime, working groups have been set up to warn and monitor in case any enterprise is going to lay off their workers. Generally, training measures are being improved to ensure that labour is competitive in the world market.

Following an assessment of the likely unemployment situation, the cabinet formulated policies which were declared to the Parliament on 20th November 1997. The unemployment alleviation plan, as a measure to support the economic stability and reliability of the economy, has three pressing policies as follows:

1. Request governmental organisations to adjust their budgets to increase employment.
2. Maintain employment.
3. Accelerate new placements.

The Ministry of Labour and Social Welfare formulated the unemployment alleviation operation plan which the cabinet voted on 9th December and 23rd December, 1997. It comprises seven measures but there are only four measures directly related to employment as follows:

1. Creation of employment in rural areas to assist the unemployed with non-permanent work by adjusting project budgets to replace machines with labour-intensive methods to employ 300,000 persons (each province is to cater for

around 5,000 persons). In this way each person was expected to receive income of about 3,000 baht per month through the year 1998

2. Reduction in the number of foreign workers within 6 months by 300,000 persons (with the focus on those who work in factories) and try to replace them with an equivalent number of Thai workers

3. Promoting overseas remittances by providing information on job vacancies and thereby increase the number of Thai workers working overseas by not less than 200,000 persons. Including workers already working overseas, it is expected that remittances will be not less than 100,000 million baht.

4. Industrial Employment Promotion measure to ensure employment of workers by methods such as improvement of job conditions, outsourcing of factories' distribution or production processes to villages in the form of home-workers, up-grading skills and new placements. Not less than 500,000 persons were expected to be employed through these measures.

The Ministry of Labour and Social Welfare expects that the goal of these four measures, of assisting not less than 1,000,000 persons, will be met.

Social Safety Nets to Alleviate Poverty

With the depth of the recession more severe and prolonged than anticipated, the development of an adequate social safety net to minimise the impact of the crisis on the most vulnerable remains a key priority.

The bulk of the additional fiscal stimulus in 1998/99 focuses on the social safety net, including job training and labour intensive projects. This programme has been carefully designed in consultation with major non-governmental organisations and labour leaders, to avoid distortions of Thailand's relatively free and well functioning labour market.

The social safety net regime is being implemented, with the support of the World Bank, the ADB, and the Overseas Economic Cooperation Fund (OECF), to provide two years of employment to a significant proportion of those who have become unemployed during the crisis and to provide free medical treatment and the improvement of rural health-care facilities.

The Government has also decided to enhance opportunities for the unemployed to become entrepreneurs through expanded micro-credit programmes and training programmes and to upgrade skills of the target group of new entrants into the labour market.

In addition, since the reduction in incomes has resulted in a sharp rise in the drop-out rate of students and an increase in child labour, the Government has provided additional budgetary allocations for the secondary education loan programme to students whose families can no longer afford tuition payments. This programme will supplement an existing grant programme for primary education financed by the ADB. The school lunch programme is also being expanded in its coverage from 30 per cent of all students to 35 per cent.

Furthermore, provisions under the Labour Protection Act will soon be implemented to provide a public compensation fund for unpaid severance payments. It will be financed by fines from violations of the Labour Protection Act while severance payments will be exempted from income tax.

Besides the above additional national spending to alleviate social impacts during this major recession, the government has also externally financed an independent project to further strengthen the social safety net. The Social Investment Programme (SIP) is aimed to help protect the unemployed, the underprivileged, and the poor from the emerging adverse social impacts. The SIP is funded by a project loan from the World Bank and the OECF that finances 90 per cent from loan disbursement and 10 per cent as the counterpart funds from the national budget. The project's management activities are also financed by grants from the UNDP and AusAID. The total cost of the SIP is approximately 22 billion baht. The activities and disbursements were expected to start in January 1999.